



A U D I T O R - G E N E R A L

The Accounting Officer
The Greater Kokstad Municipality
P.O. Box 8
KOKSTAD
4700

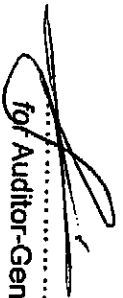
Reference: 21459REG06/07
Enquiries: Mr S Mnguni
Date: 21 January 2008

REPORT OF THE AUDITOR-GENERAL ON THE FINANCIAL STATEMENTS AND PERFORMANCE INFORMATION OF THE GREATER KOKSTAD MUNICIPALITY FOR THE YEAR ENDED 30 JUNE 2007

1. The above-mentioned report of the Auditor-General are submitted herewith in terms of section 21(1) of the Public Audit Act, 2004 (Act No. 25 of 2004 read in conjunction with section 188 of the Constitution of the Republic of South Africa, 1996 (Act No. 108 of 1996) and section 121(3) of the Municipal Finance Management Act, 2003 (Act No. 56 of 2003)(MFMA)
2. In terms of section 121(3) and 127(2) of the MFMA municipalities have to include the audit report in the municipality's annual report for tabling within seven months after the end of the financial year.
3. Until tabled as required by section 127(2) the report is **not a public document** and should therefore be treated as **confidential**.
4. As your municipality/municipal entity will be responsible for publishing the attached audit report as part of the annual report, you are required to do the following please:
 - Submit the final printer's proof of the annual report (which includes the audit report) to Mr M. Ndumo (Audit Manager) of the Auditor-General for verification of the audit-related references before it is printed or copied. Special care should be taken with the page references in your report, since an incorrect reference could have audit implications.
 - The signature at the end of the hard copy of the audit report should be scanned in when preparing to print the report. The signature *Auditor-General* in the handwriting of the auditor authorised to sign the audit report, as well as the place and date of signing and the logo should also appear at the end of the report, as in the hard copy that is provided to you. The official logo and the authorised signature will be made available to you in electronic format.

5. Please notify the Business Executive well in advance of the date on which the audit report, or the annual report containing this audit report, will be tabled at the municipality.
6. Your cooperation to ensure that all these requirements are met would be much appreciated.
7. Kindly acknowledge receipt of this letter.

Yours faithfully


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for Auditor-General

REPORT OF THE AUDITOR-GENERAL TO THE MUNICIPAL COUNCIL AND THE KWAZULU-NATAL PROVINCIAL LEGISLATURE ON THE FINANCIAL STATEMENTS AND PERFORMANCE INFORMATION OF THE GREATER KOKSTAD MUNICIPALITY FOR THE YEAR ENDED 30 JUNE 2007

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I was engaged to audit the accompanying financial statements of the Greater Kokstad Municipality (municipality) which comprise the balance sheet as at 30 June 2007, income statement and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes, as set out on pages 3 to 17.

Responsibility of the accounting officer for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the Institute of Municipal Finance Officers (IMFO) and in the manner required by the Municipal Finance Management Act, 2003 (Act No. 56 of 2003) (MFMMA). This responsibility includes:

- designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error
- selecting and applying appropriate accounting policies
- making accounting estimates that are reasonable in the circumstances.

Responsibility of the Auditor-General

3. As required by section 188 of the Constitution of the Republic of South Africa, 1996, read with section 4 of the Public Audit Act, 2004 (Act No. 25 of 2004) (PAA) and section 126(3) of the MFMA, my responsibility is to express an opinion on these financial statements based on my audit in accordance with the International Standards on Auditing. Because of the matters discussed in the Basis for disclaimer of opinion paragraphs, however, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Basis of accounting

4. The municipality's policy is to prepare financial statements on the entity-specific basis of accounting as described in accounting policy note 1 to the financial statements.

Basis for disclaimer of opinion

Account receivables

5. I was unable to verify debtor balance of R46,9 million for valuation and completeness due to the following:
 - Individual billings could not be traced to the individual debtor accounts to confirm that all invoices were properly accounted for.
 - As disclosed in note 9 to the annual financial statements, an amount of R5,3 million was raised as a provision for bad debts against debtors totalling R34,7 million. This provision is based on the council's policy which requires a provision of 15 per cent of outstanding debts at year-end. However, my review of debtors indicated that the provision was not adequate because debtors amounting to R45,7 million were outstanding for more than 120 days at 30 June 2007.

Fixed assets

6. I was unable to verify the fixed assets balance of R16,6 million for completeness and valuation due to the following:

- Included in fixed assets are redeemed, transferred or written-off assets amounting to R7,6 million for which no supporting documentation could be provided.
- Included in loans redeemed and other capital receipts are repayments of R8,5 million for which no supporting documentation could be provided. In addition, the amount of R8,5 million does not agree to the amount of R1,5 million for loans redeemed or written off during the year.
- Included in loans redeemed and other capital receipts are contributions from operating income of R3,0 million for which no supporting documentation could be provided. In addition, there were no contributions from operating income as per the analysis of operating income and expenditure.
- Included in loans redeemed and other capital receipts are external contributions of R40 000 for which no supporting documentation could be provided and no external contributions are disclosed in the analysis of operating income and expenditure.
- Included in loans redeemed and other capital receipts are grants and subsidies of R12 million. However, the amount does not agree to the R25,1 million for assets financed by grants reflected as per the municipality's schedules provided for the audit.
- No reconciliation was performed between net fixed assets of R16,6 million (per appendix C to the financials) and external and internal loans of R17,3 (per appendix B to the financials), resulting in an unexplained difference of R749 000.

Leave pay provision

7. Certain leave days taken as per approved leave forms and leave accruals in terms of the applicable leave policies were not correctly recorded on the leave cards. Consequently, I was unable to verify completeness and valuation of the leave pay provision disclosed as R2,4 million.

Cash and bank

8. The year-end bank reconciliation reflects an unreconciled difference of R215 000 for which no adequate explanation or supporting documentation could be provided. Consequently, the cash and bank balance of R807 000 could not be verified for valuation and completeness.

Creditors

9. Included in the accounts payable is an amount of R1,5 million for interest and redemption for which no supporting documentation or adequate explanations could be provided. Consequently, I was unable to verify the balance for existence, obligation and valuation.

Value-added tax (VAT)

10. The municipality failed to perform adequate and proper VAT reconciliations during the year and had no allocation formula in place to distinguish between vatiable and non-

variable supplies. Consequently, the amount of R12,5 million relating to the VAT debtor could not be verified for existence, completeness and valuation.

DISCLAIMER OF OPINION

11. Because of the significance of the matters described in the Basis for disclaimer of opinion paragraphs, I have been unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on the financial statements of the Greater Kokstad Municipality. Accordingly, I do not express an opinion on the financial statements.

OTHER MATTERS

I draw attention to the following matters that are ancillary to my responsibilities in the audit of the financial statements:

12. Material corrections made to the financial statements submitted for audit

The financial statements, approved by the accounting officer and submitted for audit on 31 August 2007, have been revised in respect of the following misstatements identified during the audit:

- The provision for bad debts was understated by R3,3 million as no provision was made for the Sisonke District Municipality debtor. To correct the misstatement the provision for doubtful debts and the bad debt expense was increased by that amount.
- The misclassification of certain fixed assets resulted in an overstatement of fixed assets and an understatement of accounts receivable by R4,2 million. The misstatement was corrected by decreasing fixed assets and increasing accounts receivable by that amount.
- The financial statements was corrected by decreasing the provision for bad debts by R2,4 million for indigent debtors that were provided for but not written off.
- Indigent debtors of R3,3 million were not written off during the year, resulting in an overstatement of account receivables and an understatement of written-off indigent debtors by that amount. The misstatement was corrected by decreasing accounts receivable and increasing the expenditure by R3,3 million.
- No interest was transferred to statutory funds. As a result, statutory funds and interest paid were both understated by R467 000. The misstatement of the financial statements was corrected by increasing the statutory funds and interest paid by that amount.
- Accounting errors were corrected as follows:
 - An overstatement of the VAT debtor was corrected by decreasing the accumulated surplus and accounts receivable by an amount of R5,6 million.
 - An overstatement of fixed assets and the accumulated surplus was corrected by decreasing the fixed assets and accumulated surplus by an amount of R3,4 million.
 - An overstatement of the leave pay provisions was corrected by decreasing the provision for leave pay expense and provisions by an amount of R485 000.

- An understatement of grant income and an overstatement of accounts payable were corrected by increasing the grant income and decreasing accounts payable by an amount of R494 000.
- An understatement of accounts payable and payments for goods and services caused by unaccounted liabilities was corrected by increasing the accounts payable and payments for goods and services by R5,5 million.
- An understatement of the accumulated surplus and VAT expense caused by a prior year error was corrected by increasing the accumulated surplus and VAT expense by an amount of R379 000.
- An understatement of accounts payable and salaries and wages was corrected by increasing the accounts payable and salaries and wages by an amount of R1,1 million.
- An overstatement of accounts payable and an understatement of accumulated surplus were corrected by decreasing the accounts payable and increasing the accumulated surplus by an amount of R1,9 million.
- An understatement of the leave pay provision in the income statement and the leave pay provision was corrected by increasing the provision for leave pay by an amount of R341 000.

- Misstatements in the disclosure notes were corrected by decreasing the councillors' allowance by R779 934, increasing the fixed assets by R352 648, increasing VAT allocation by R2,6 million, and increasing houses transferred by R20,7 million.

13. Internal control

Section 62(1)(c)(i) of the MFMA states that the accounting officer must ensure that the municipality has and maintains effective, efficient and transparent systems of financial and risk management and internal control. The table below depicts the root causes of the matters indicated, as they relate to the five components of internal control. In some instances deficiencies exist in more than one internal control component.

Reporting item	Control environment	Assessment of risks	Control activities	Information and communication	Monitoring
Basis for disclaimer of opinion					
Accounts receivables			X		X
Fixed assets			X		X
Leave pay provision			X		X
Cash and bank			X		X
Creditors			X		
Value-added tax			X		
Other matters					
Material corrections to the financial statements			X		X

14. Unaudited supplementary schedules

The supplementary information set out on pages 18 to 23 does not form part of the financial statements and is presented as additional information. I have not audited these schedules and, accordingly, I do not express an opinion on them.

OTHER REPORTING RESPONSIBILITIES

Reporting on performance information

15. I was engaged to audit the performance information.

Responsibility of the accounting officer for the performance information

16. In terms of section 12(1)(3)(c) of the MFMA, the annual report of a municipality must include the annual performance report of the municipality prepared by the municipality in terms of section 46 of the MSA.

Responsibility of the Auditor-General

17. I conducted my engagement in accordance with section 13 of the PAA read with *General Notice 646 of 2007*, issued in *Government Gazette No. 29919 of 25 May 2007* and section 45 of the MSA.

18. In terms of the foregoing, my engagement included performing procedures of an audit nature to obtain sufficient appropriate evidence about the performance information and related systems, processes and procedures. The procedures selected depend on the auditor's judgement.

19. I believe that the evidence I have obtained is sufficient and appropriate to provide a basis for the audit findings reported below.

Audit findings (performance information)

20. Non-compliance with regulatory requirements

20.1 No finalised performance measurement system

The municipality did not develop and implement mechanisms, systems and processes for auditing the results of performance measurements as part of its internal audit processes, as required in terms of section 45 of the MSA.

20.2 No performance reports compiled during the year

The municipality did not submit an annual performance report as required by section 46 of the MSA. Consequently, the municipality's performance against any measurable performance objectives was not audited, as required by section 45(b) of the MSA.

20.3 Integrated development plan (IDP)

The following shortcomings were noted with regard to the IDP:

- No evidence could be provided for audit purposes to confirm community involvement in the IDP review, as required by section 28 of the MSA.

- The development strategies of the municipality were not aligned with national or provincial requirements in terms of section 26(d) of the MSA.
- The financial plan per the IDP did not agree to the budget.
- The IDP did not disclose the performance indicators or targets against which the performance of the municipality should be measured, as required in terms of section 26(f) of the MSA.
- The progress of projects in the service delivery and budget implementation plan was not monitored on a regular basis.
- The integrated development process plan did not assign responsibility to the municipal manager for the drafting of the IDP, as required by section 30(b) of the MSA.

APPRECIATION

21. The assistance rendered by the staff of the Greater Kokstad Municipality during the audit is sincerely appreciated.

Heather - Smaane
Pietermaritzburg

18 January 2008



AUDITOR-GENERAL